

JLBC **MONTHLY FISCAL HIGHLIGHTS** **February 2007**

January General Fund revenue collections were \$1.01 billion, or 9.8% above January 2006. This amount was \$27.0 million above the original enacted FY 2007 forecast. For the fiscal year-to-date, collections are \$104.3 million above the original enacted FY 2007 forecast. (*See Table 3 on page 2.*)

The January collections can also be viewed from the revised FY 2007 forecast that was released last month as part of the January JLBC Baseline. That forecast raised the projected level of FY 2007 collections by \$295 million. When measured against this higher forecast, January revenues were \$(7.5) million below target.

While overall January collections were strong at 9.8%, among the major tax categories performance was mixed. Individual income tax collections increased 17.9%, and corporate income tax revenues were 9.6% above last year. Sales tax collections, however, only increased 4.7%, the result of only 1.0% growth in retail sales collections. For the year-to-date, total collections are 8.7% above last year. (*See Table 8 on page 10 for details.*)

In other fiscal news this month, the JLBC met on February 6th (*pages 4 – 5*).

The Monthly Fiscal Highlights also include a summary of recent statutory reports to JLBC (*pages 5 – 8*). Of note, the Arizona Department of Education increased its FY 2007 surplus estimate from \$9.0 million to \$10.1 million, while the

Department of Corrections increased its FY 2007 shortfall estimate from \$(8.7) million to \$(14.2) million.

In addition, the Monthly Fiscal Highlights include an update on the following budget issues (*pages 8 – 9*):

- As the result of a 2003 criminal case in which a Scottsdale-based company forfeited \$28.7 million to the state, the Attorney General has allocated \$25.6 million. Among the major items, the Attorney General plans to distribute \$17.7 million to the Department of Public Safety for a crime lab in Tucson.
- The JLBC Staff released its latest calculation of the state's appropriation limit. The Arizona Constitution limits the appropriations of certain state revenues to no more than 7.41% of personal income. Under the JLBC Baseline, appropriations would be 6.83% of personal income in FY 2007 and 6.45% in FY 2008.
- The JLBC Staff released its calculation of the Truth in Taxation (TNT) adjustments to property tax rates. Each year these rates are adjusted to offset increases in the value of existing property. Due to 8.6% growth in existing property values, the property tax rate for unified school districts would be reduced by 27.5¢ in FY 2008. Since the 8.6% rate of growth was higher than forecasted, the JLBC Baseline would need to be increased by \$19.0 million to fully fund the TNT adjustments.

Table of Contents

<u>Page #</u>	<u>Page #</u>
January Revenues.....	2
Recent Economic Indicators	2
 <u>February 6 JLBC Meeting Summary</u>	
- Attorney General – Uncollectible Debts.....	4
- Attorney General – Allocation of Settlement Monies.....	4
- ADC – Transfer of Appropriations	4
- ADE – Kinder Morgan Settlement	4
- DEQ – Water Quality Permit Processing Times.....	5
- Land Dept. – Central Arizona Project Water Delivery	4
- DPS – Arizona Public Safety Communications Advisory Commission	4
- DPS – Microwave Communication System	4
- DOR – BRITS Contract Amendment	5
- ASU – School of Journalism	5
 <u>Summary of Recent Agency Reports</u>	
- AHCCCS – Graduate Medical Education Residencies.....	5
- AHCCCS – Redetermination Policy.....	5
- Comm. Colleges/DES/ADE/Universities – Public Programs Eligibility	5
 <u>Summary of Recent Agency Reports (cont'd)</u>	
- Corp. Commission – Corporations Division Filings	6
- ADC – Community Accountability Pilot Program.....	6
- ADC – Report on Expenditures.....	6
- ADC – Transition Program	6
- ACJC – Methamphetamine Interdiction Efforts.....	6
- ADE – Budget Status Report.....	6
- ADE – Excess Utilities Spending.....	6
- DHS – Federal Vaccines Program.....	7
- DHS – MethSMART Prevention Program.....	7
- DPS – Staffing Levels	7
- ABOR – Differentiated Tuition.....	7
- ABOR/UofA – Phoenix Medical Campus	7
- ADOT – MVD Wait Times.....	8
- ASU – Guaranteed Tuition Pilot Program.....	8
- DWR – Assured and Adequate Water Supply Fees	8
 <u>Other Issues</u>	
- Attorney General Settlement Allocation	8
- State Appropriations Limit	9
- Truth in Taxation K-12 Property Tax Rates.....	9

JANUARY REVENUES

Sales Tax collections were \$440.0 million in January, or 4.7% above last January. The following table displays the January and year-to-date growth rates for the major categories.

Table 1**Sales Tax Growth Rates**

	<u>January</u>	<u>Year-to-Date</u>
Retail	1.0%	4.1%
Contracting	14.4%	16.6%
Utilities	0.9%	10.4%
Use	1.9%	4.2%
Restaurant & Bar	8.5%	9.4%

Overall, sales collections continued to grow at a slower rate than prior months in FY 2007. The slower growth was largely driven by a weak month for retail collections, the result of poor holiday shopping season sales. For the month, revenues were \$(7.0) million below the June 2006 forecast.

Individual Income Tax collections were \$544.3 million in January, or 17.9% above last year. *Table 2* displays the January and year-to-date growth rates for the individual income tax categories.

Table 2**Individual Income Tax Growth Rates**

	<u>January</u>	<u>Year-to-Date</u>
Withholding	17.5%	9.1%
Estimated + Final Payments	31.4%	26.0%
Refunds	254.8%	78.6%

Withholding collections for the month were strong, as were estimated payments. The gains in these categories were somewhat offset by the continued high growth in refunds. Overall, monthly revenues were \$35.6 million above the June 2006 forecast.

Corporate Income Tax collections were \$37.3 million in January, or 9.6% above last year. For the month, corporate income tax revenues were \$(2.0) million below the June 2006 forecast.

RECENT ECONOMIC INDICATORS

The first estimates for 2006's 4th quarter indicated that **U.S. Gross Domestic Product (GDP)** growth increased to a 3.5% annual rate, up from the 2.0% pace posted in the 3rd quarter. Increases in personal consumption expenditures, net exports, and federal, state, and local government spending contributed to the growth acceleration, while spending slowed for nonresidential structures and software.

U.S. semiconductor billings reached new highs in 2006. Although December sales (3-month moving average) slipped (4.2)% from the prior period, they increased 4.5% on a year-over-year basis. For all of 2006, the Semiconductor Industry Association (SIA) reported that American manufacturers totaled \$45.0 billion in sales, a 12.4% increase from 2005.

After dipping in late 2006, prices were moving higher again at the start of 2007. The **U.S. Consumer Price Index (CPI)** (3-month moving average) increased 0.1% in January, while the corresponding year-over-year increase was 2.2%. Medical care and food and beverages were among the categories showing sharp price increases in January. Excluding the impact of food and energy prices, the core CPI rose 2.7% from a year ago.

The Conference Board's **U.S. Consumer Confidence Index** climbed 0.3% in January. Consumers' view of labor market prospects improved and their overall assessment of current conditions was brighter, but the outlook for the next 6 months was less sanguine than in December.

The **U.S. Index of Leading Economic Indicators** edged up 0.1% in January. The improvement was led by consumer sentiment, stock prices, and declining unemployment insurance claims, while manufacturing hours worked, new orders, building permits, and interest rates were among the factors making negative contributions.

Arizona's residential real estate market continued to languish. Statewide, the number of single-family **residential building permits** (3-month moving average) dropped (2.0)% in December and was down (48.4)% on a year-over-year basis. Multi-family permits decreased (2.3)% from the prior month and declined (48.9)% from a year ago. For all of 2006, 65,752 housing units were authorized in Arizona, a decrease of

Table 3

General Fund Revenues
Compared to Enacted and Revised Forecasts and FY 2006 Collections
(\$ in Millions)

	<u>FY 2007 Collections</u>	<u>Difference From June 2006 Forecast</u> ^{1/}	<u>Difference From Jan 2007 Forecast</u> ^{2/}	<u>Difference From FY 2006</u>
February	\$ 1,012.1	\$ 27.0	\$ (7.5)	\$ 90.4
Year-to Date	\$ 5,558.4	\$ 104.3	\$ (7.5)	\$ 443.7

^{1/} Originally enacted FY 2007 budget (June 2006)

^{2/} JLBC January Baseline Budget

(27.6)% from 2005. The total value of residential permits issued was \$1.1 billion in 2006, a (22.1)% decrease from 2005's \$1.4 billion total.

The Realty Studies group at Arizona State University estimated that the Greater Phoenix **single-family median resale home price** rose 1.6% in January to \$260,000. The number of single-family homes sold declined (2.2)% from the prior month and by (14.1)% on a year-over-year basis.

The **townhouse-condominium median price** was \$175,000 in January, unchanged from December and 6.1% higher than a year ago. The number of units sold dipped (3.4)% from December to 850 in January, which was a (30.6)% decrease from a year ago.

The **Arizona Business Conditions Index** dropped (2.6)% to 53.4 in January, which was still above the mark of 50 associated with an expanding economy. The production and purchases categories fell sharply, but the new orders component regained some of the ground it lost in recent months.

The Behavior Research Center's **Arizona Consumer Confidence Index** started the year with a reading of 106.3 for 2007's 1st quarter, a 0.9% increase from the 4th quarter of 2006. Although consumers in the Phoenix area were growing more optimistic, confidence was falling in Tucson and the rural regions of the state. Overall, consumers' assessment of current business conditions was mostly unchanged, while their perspective on the job market dimmed from the previous quarter.

The number of **air passengers** counted at Phoenix Sky Harbor International Airport dipped (0.1)% on a year-over-year basis in December. For all of 2006, more than 41.4 million passengers flew through the airport, a 0.5% increase from 2005.

The **Department of Corrections' inmate population** increased by an average of 37 inmates per month from November through January. The total population increased by 2,385 inmates from a year ago.

Table 4

RECENT ECONOMIC INDICATORS

<u>Indicator</u>	<u>Time Period</u>	<u>Current Value</u>	<u>Change From Prior Period</u>	<u>Change From Prior Year</u>
Arizona				
- Unemployment Rate	December	4.1%	0.0%	(0.6)%
- Jobs	December	2.72 million	0.6%	4.5%
- Contracting Tax Receipts (3-month average)	Nov-Jan	\$84.3 million	3.7%	13.6%
- Retail Sales Tax Receipts (3-month average)	Nov-Jan	\$178.9 million	12.1%	3.0%
- Residential Building Permits - (3-month moving average)				
Single-unit	Oct-Dec	2,969	(2.0)%	(48.4)%
Multi-unit	Oct-Dec	479	(4.1)%	(48.9)%
- Greater Phoenix Existing Home Sales				
Single-Family	January	4,520	(2.2)%	(14.1)%
Townhouse/Condominium	January	850	(3.4)%	(30.6)%
- Greater Phoenix Median Home Sales Price				
Single-Family	January	\$260,000	1.6%	1.2%
Townhouse/Condominium	January	\$175,000	0.0%	6.1%
- Arizona Tourism Barometer	December	107.5	2.1%	2.1%
- Phoenix Sky Harbor Air Passengers	December	3.41 million	(0.1)%	(0.9)%
- Arizona Average Natural Gas Price (\$ per thousand cubic feet)	November	\$9.05	46.0%	1.9%
- Leading Indicators Index	November	119.0	(0.1)%	(1.1)%
- Business Conditions Index (>50 signifies expansion)	January	53.4	(2.6)%	(15.3)%
- Consumer Confidence Index	1 st Quarter 2007	106.3	0.9%	(3.7)%
- Business Leaders Confidence Index	1 st Quarter 2007	51.9	7.9%	(13.4)%
- Arizona Personal Income	3 rd Quarter 2006	\$195.4 billion	1.8%	7.1%
- Arizona Population	July 1, 2006	6.17 million	3.6%	3.6%
- AHCCCS Recipients	February	1,024,916	(0.5)%	(1.9)%
- TANF Recipients	December	84,237	0.0%	(13.7)%
- DOC Inmate Growth (3-month average)	Nov-Jan	35,820	37 inmates	2,385 inmates
United States				
- Gross Domestic Product (seasonally adjusted annual growth rate)	4 th Quarter 2006	\$11.5 trillion	3.5%	3.4%
- Consumer Confidence Index	January	110.3	0.3%	3.3%
- Leading Indicators Index	January	138.5	0.1%	(0.1)%
- U.S. Semiconductor Billings (3-month moving average)	Oct-Dec	\$3.80 billion	(4.2)%	4.5%
- Consumer Price Index (3-month moving average)	Nov-Jan	201.9	0.1%	2.2%

The number of TANF recipients was virtually unchanged in December. The 84,237 who received benefits were just 9 more than the November total but (13.7)% fewer than the number reported a year ago. The **AHCCCS caseload** decreased (0.5)% in February from the prior month and was (1.9)% below the level from a year ago.

JLBC MEETING

At its February 6, 2007 meeting, the Joint Legislative Budget Committee considered the following issues:

Attorney General – Review of Uncollectible Debts – The Committee gave a favorable review to the Attorney General's listing of \$16.8 million in uncollectible debt from FY 2005, with the exception of \$3.4 million involving a debtor that can not be located and \$3.4 million involving a now-defunct corporation that secured a loan from the Department of Commerce. The favorable review by the Committee will allow the State Comptroller to remove debt, certified by the Attorney General (AG) as uncollectible, from the state accounting system. In addition to the favorable review, the Committee requested from the Department of Commerce more information on the loan to the now-defunct corporation.

Attorney General – Review of Allocation of Settlement Monies – The Committee gave a favorable review of the allocation plans from the Sony BMG settlement agreement and the Deed and Note Traders consent decree. The Sony BMG settlement was due to the company placing anti-copying software on certain CDs without adequate disclosures to consumers, which exposed some consumers to computer viruses. The Deed and Note Traders Consent Decree settlement was due to the company operating fraudulent home ownership programs targeted to consumers facing foreclosure or with bad credit. The General Appropriation Act contains a footnote that requires JLBC review of the expenditure plan for settlement monies over \$100,000.

Department of Corrections – Consider Approval and Review of Requested Transfer of Appropriations – The Committee approved a transfer of \$7.5 million to the Overtime/Compensatory Time (OT/CT) line item. Of this, \$6 million will be transferred from the Department of Correction's employee benefits line item. The remaining \$1.5 million will come from the County Jail Beds Special Line Item. These excess monies occurred due to the cancellation of a contract with the Coconino County jail for 88 beds. The Committee also deferred action on transferring monies from the Private Prison Per Diem SLI to the Provisional Beds SLI until the department negotiates a contracted rate for replacement beds. The agency had requested a transfer of \$12.3 million.

Department of Education – Review of Kinder Morgan Settlement – The Committee gave a favorable review to the Department of Education request to provide \$306,400 in additional Basic State Aid Funding to school districts in Pinal County due to assessment evaluation changes pertaining to the recent Kinder Morgan Settlement. At two earlier JLBC meetings, the Committee favorably reviewed similar requests

pertaining to school districts in Yuma, Cochise, and Maricopa Counties. Statute requires that the state make up the lost revenues as a result of the revised assessment valuation.

Arizona Department of Environmental Quality – Review of Water Quality Permit Processing Times – The Committee gave a favorable review to the Department of Environmental Quality's (DEQ) report on water quality permit processing times for FY 2006 and FY 2007. In FY 2006 the department processed approximately 2,900 water quality permit applications, with an average staff time of 30 hours per permit, and a total cost of \$4.2 million. In FY 2007, DEQ expects to process about 3,150 permits, with an average permit time of 31 hours and a total cost of \$5.1 million.

In addition to the favorable review, the Committee also asked DEQ to report by February 26, 2007 on its rationale for not using \$200,000 allocation from the Water Quality Fee Fund in FY 2007 for additional contract permitting staff, given the increase in applications.

State Land Department – Consider Approval of Amended Contract for Permanent Central Arizona Water Delivery – The Committee approved the State Land Department request to amend a contract originally approved by the Committee in 1986 which allows the agency to purchase approximately 32,000 acre-feet of Municipal and Industrial (M&I) CAP water to maintain the value of trusts lands in Maricopa, Pinal and Pima counties. The amended contract extends the period of the contract from 50 to 100 years. This amendment does not change the financial obligations of the State nor does it change the amount of water purchased by the Land Department.

Department of Public Safety – Quarterly Review of Arizona Public Safety Communication Advisory Committee – The Committee gave a favorable review of first quarter expenditures for the Public Safety Communication Advisory Commission (PSCC) statewide interoperability project. First quarter expenditures totaled \$209,700 of the nearly \$4.3 million funding. A technical writer position was filled, bringing the total staff to 7 of 9 positions. The Arizona PSCC was established to develop a statewide standard based interoperability system that allows public personnel from one agency to communicate, via mobile radio, with personnel from other agencies. The PSCC timeline targets the establishment of a financing and development plan for the system by July 2008.

Department of Public Safety – Review of Microwave Communication System Upgrade Expenditures and Progress – The Committee gave a favorable review to the Department of Public Safety (DPS) on its expenditures and progress of the upgrade to its microwave communication system. The microwave system is the backbone of the DPS statewide radio system. The system provides dispatch control of radio base stations and connects 53 remote radio communication sites and 20 state office locations.

In addition to the favorable review, the Committee requested the Department include the following with its June 30, 2007 statutory report: 1) an updated cost estimate on the southern loop of the project and the entire project; 2) an updated expenditure plan and project timeline for the entire project which addresses the lack of Homeland Security monies. The Committee also requested an explanation directly from the Arizona Department of Homeland Security regarding why the project has not received federal homeland security monies so far in FY 2007.

Arizona Department of Revenue – Review of Business Reengineering/Integrated Tax System Contract Amendment – The Committee gave a favorable review of the Department of Revenue's request for a \$2.2 million contract amendment to continue operation of the Business Reengineering/Integrated Tax System (BRITS) data center. The amendment extends the vendor's operation of the system for 1 year from October 2007 to September 2008. Statute requires any Committee review of any BRITS contract extension or modification. BRITS is the computer system being implemented by the DOR to further automate and integrate their separate tax systems. It was designed to improve enforcement and ultimately increase revenues to the state.

Arizona State University – Review of Walter Cronkite School of Journalism – The Committee gave a favorable review of Arizona State University's (ASU) agreement with a private developer to design and construct the Cronkite School of Journalism/KAET Channel 8 project.

The project involves the construction of a 217,700 square-foot 6-story building that will cost approximately \$71 million. The construction of the school will be financed with proceeds from the \$188 million bond approved by City of Phoenix voters to construct and renovate several buildings at ASU's Downtown Phoenix Campus. ASU estimates that beginning in FY 2009, 1,800 students attending the Downtown Campus would be enrolled in the School of Journalism.

SUMMARY OF RECENT AGENCY REPORTS

AHCCCS – Report on Graduate Medical Education Residency Positions – Pursuant to Laws 2006, Chapter 331, the Arizona Health Care Cost Containment System (AHCCCS) has submitted a report on the number of residency positions created by the additional \$4,000,000 General Fund (\$12,000,000 Total Funds) appropriated for Graduate Medical Education in the FY 2007 budget. The agency indicates that stakeholder meetings were conducted early in the fiscal year to agree upon a methodology for distributing the funding. On January 12, 2007, this methodology was filed as a proposed Rule and is expected to become effective in May or June 2007. Monies will then be distributed to state hospitals as soon as the Rule is finalized. Due to the timing of these distributions, AHCCCS indicates that no data is currently available regarding the number of positions funded with the FY 2007 appropriation for Graduate Medical Education. After distributing these monies this summer, AHCCCS anticipates

being able to report on the number of residency positions funded by February 1, 2008.

AHCCCS – Report on Redetermination Policy – Pursuant to Laws 2006, Chapter 331, AHCCCS has submitted a report to the Joint Legislative Budget Committee on the effects of shortening the redetermination period to 6 months for Temporary Assistance for Needy Families (TANF) Cash Benefit clients age 21 or older.

According to AHCCCS' report, a total of 49,959 letters were sent during a 7-month period (June 2006 through December 2006) to redetermine eligibility. Of that total, their current status is as follows:

36,488 (73%) – Interviewed

34,865 (95.6%) – Interviewed and retained benefits

A total of 12,408 individuals were terminated because they did not show up for their redetermination interview. Approximately 53% of these individuals, however, returned to the AHCCCS program within 3 months of their initial termination.

Comm. Colleges/Dept. of Economic Security/Dept. of Education/Universities – Public Programs Eligibility Report – As enacted by voters at the November 2006 election, Proposition 300 limits participation in the Adult Education and Child Care programs to citizens, legal residents, or other persons lawfully present in the United States. Proposition 300 also prohibits persons who are not citizens, legal residents, or otherwise lawfully present from being entitled to classification as an in-state or in-county resident for university or community college tuition purposes, or from receiving state funded financial assistance. The proposition requires the state agencies administering the programs described above (and the Family Literacy Program) to report twice annually to the Joint Legislative Budget Committee the total number of persons qualifying for these programs, as well as the number of persons deemed ineligible due to their citizenship, residency, or immigration status.

Reports were received from the universities, community colleges, and the Department of Economic Security. The Arizona Department of Education, however, did not provide a report. The reporting entities indicated that because the effective date of this legislation was December 7, and the first report was due December 31, there is no information available to report, as many of these institutions previously did not record this type of information. Because of early spring registrations, however, Cochise County Community College District provided information on the number of students entitled to classification as an in-county student, and the number of students who applied for financial aid. Cochise reports that none of their students were ineligible either for classification as an in-county resident or for financial aid because of citizenship status. The eligibility information submitted by Cochise was based on self-verification from students.

Currently, the universities and the community colleges are developing guidelines for implementation of Proposition 300. The Arizona Department of Education has indicated that they are currently waiting for guidance from the Attorney General before enacting implementation measures. The Department of Economic Security, under its currently adopted set of rules and policies, already requires proof of citizenship status for the Child Care program. The next report from all agencies affected by Proposition 300 is due June 30.

Corporation Commission – Report on Corporations Division Filings – Pursuant to a footnote in the General Appropriation Act, the Corporation Commission submitted a quarterly report on the status of reducing processing delays in its Corporations Division.

For expedited filings, the amount of time required to process the filings fell from an average of 23 business days on March 25, 2005, to 4.2 business days on December 31, 2006. At the end of the first quarter of FY 2007, the turnaround time was 3.6 business days. The commission's goal for processing expedited filings is 5 business days or less.

For regular filings, the amount of time required to process the filings fell from an average of 68 business days on March 25, 2005, to 43 business days on December 31, 2006. At the end of the first quarter of FY 2007, the turnaround time was 34.8 business days. The commission's goal for processing regular filings is 30 business days or less.

The commission updated its corporate filings reporting to include the processing times for Annual Reports, which has changed the results of its quarterly reports as well as its reporting baseline.

Department of Corrections – Report on Community Accountability Pilot Program – A.R.S. § 41-1609.05 required the Arizona Department of Corrections to establish a Community Accountability Pilot Program. Statute authorizes the department to contract with a private or non-profit entity to provide supervision and treatment services for eligible offenders who have violated the terms and conditions of community supervision.

The department awarded the contract to Redman Investment Group and the program began on April 13, 2006. As of the program's inception in January 2007, a total of 101 eligible offenders have been referred to the Community Accountability Pilot Program. Of those referred, 71 offenders, or 70.3%, were terminated from the program due to committing new crimes, failed urinalysis tests, absconding, or failure to report to parole officers. To date, program participants have spent 1,038.1 hours in programming and counseling services.

Department of Corrections – Report on Expenditures – Pursuant to Laws 2006, Chapter 344 (General Appropriation Act), the Arizona Department of Corrections (ADC) is required to report on the monthly and year-to-date expenditures for the current and prior fiscal year. The report

is also to include potential shortfalls, any estimated surpluses to offset the shortfalls, and a plan for eliminating the shortfall.

Based on the December 2006 report, the department is now estimating a FY 2007 shortfall of \$(14.2) million, which matches the Executive supplemental request. This projected shortfall is an increase of \$5.5 million from last month, when the department projected a shortfall of \$(8.7) million.

Department of Corrections – Report on Transition Program – Pursuant to A.R.S. § 31-285B, the Arizona Department of Corrections (ADC) is required to submit a quarterly report that details the cost reductions to the department from an inmate early release Transition Program. Statute requires ADC to contract with a private or nonprofit entity to provide eligible drug offenders with transition services.

The ADC Transition Program began in March 2004. From October 1 through December 31, 2006, the department reports that 127 inmates successfully completed the Transition Program and their term of community supervision. As a result, there were 8,812 bed days saved and \$149,804 in savings. Since program inception, a total of 754 inmates, or 55.8% of program participants, successfully completed the Transition Program and their term of community supervision with savings of 84,806 bed days and \$1,441,700. In total, 84.3% of participants that completed the program have remained in the community without committing additional offenses.

Arizona Criminal Justice Commission – Report on Statewide Methamphetamine Interdiction Efforts – Pursuant to Laws 2006, Chapter 337, the Arizona Criminal Justice Commission (ACJC) is required to report quarterly with a summary outlining the use and effectiveness of \$3 million appropriated in FY 2007 for increased methamphetamine interdiction efforts by the counties.

All monies have been allocated to counties based on the formula in Chapter 337. ACJC reported that as of December 31, 2006, \$5,600 had been spent. Maricopa County reported the expenditure of \$2,300 on consulting and contractual expenses. Maricopa County has taken on the role of project coordinator for the Arizona Meth Project (AMP), a multimedia public service program targeting youth, young adults and their parents. Maricopa County reported finalizing intergovernmental agreements with 7 counties to use their methamphetamine funding for AMP.

Department of Education – Budget Status Report – Pursuant to A.R.S. § 35-131(D) and a footnote in the FY 2007 General Appropriation Act, the Arizona Department of Education (ADE) recently provided an update regarding its budget status for FY 2007. In that report, ADE estimates that it will experience a \$10.1 million net funding surplus for FY 2007. ADE had previously reported a surplus of \$9.0 million.

Department of Education – Excess Utilities Report – Pursuant to A.R.S. § 15-910.03(C), the Arizona Department

of Education (ADE) recently provided a report regarding school district Excess Utilities funding. The report shows that 135 school districts (out of 238 total statewide) budgeted for Excess Utilities for FY 2007. Of that total, 114 submitted a statutorily required Excess Utilities report to ADE for FY 2007 and 21 did not. The 114 respondents reported total budgeted utility costs of \$211 million for FY 2007, of which \$89 million was budgeted as “Excess Utilities.” School districts can increase their local property taxes to fund “Excess Utilities” through FY 2009 pursuant to A.R.S. §15-910(A-F).

Department of Health Services – Report on Federal 317 Vaccines Program – Pursuant to a footnote in the General Appropriation Act, the Department of Health Services (DHS) is reporting to the Committee on the amount of federal monies received for FY 2007 for the Federal 317 vaccines program. The Federal 317 Vaccines program provides immunizations to children in public settings, such as malls and clinics. The department reports that as of February 1, it has received \$2,089,800 in Federal 317 monies.

In FY 2006, the department received \$2,226,400 in Federal 317 Vaccines funding.

Department of Health Services – Report on MethSMART Prevention Program – Pursuant to Laws 2006, Chapter 337, Section 5, the Department of Health Services has submitted a quarterly report on the effectiveness of the department’s curriculum based methamphetamine prevention services. In FY 2007, \$500,000 was appropriated to the department for methamphetamine prevention programming for youths. Grants were provided to 15 Boys and Girls Clubs across the state to implement the MethSMART prevention program.

The MethSMART program provides separate curriculum for children, youth, and teens and also includes a workshop for parents. The department reports that 1,415 youth and teens have participated in the program since it began in October 2006. Approximately 1,238 of those children and youth completed the entire MethSMART curriculum for their age group. The department reports that there was a 13-21% increase in youth’s knowledge about methamphetamine following participation in the program.

Arizona Department of Public Safety – Report on Staffing – Pursuant to Laws 2006, Chapter 344 (General Appropriation Act), the Arizona Department of Public Safety (DPS) is required to report quarterly on staffing levels for both crime lab and sworn personnel. The department indicates they currently have 143 authorized crime lab positions. Of this amount, 124 (or 86.7%) are currently filled, as compared to 126 filled at the end of the prior quarter.

DPS currently has 1,359 authorized sworn full-time positions, including 100 authorized sworn positions for the Gang and Immigration Intelligence Enforcement Mission (GITEM). The additional 100 GITEM positions were not reflected in the 1st quarter report. Of the 1,359 authorized sworn positions, 1,119 (or 82.3%) are currently filled. Of the 169 new

positions funded in the last 2 years, DPS has realized a net increase of 37 filled positions.

Arizona Board of Regents – Report on Differentiated Tuition for Students Above the Credit Hour Threshold – A footnote in the General Appropriation Act requires the Arizona Board of Regents (ABOR) to report to the JLBC on its plan for establishing, pursuant to A.R.S. § 15-1626, a differentiated tuition and fee rate structure for students who have earned credit hours in excess of the credit hour threshold. The credit hour threshold is set at 155 hours in FY 2007, 150 hours in FY 2008, and 145 hours from FY 2009.

In November 2006, ABOR approved a tuition surcharge equal to 20% of the resident undergraduate tuition for the 2007-2008 academic year for all resident and non-resident undergraduate students in excess of the 150 credit hour threshold. For students taking 1 to 6 credit hours, the surcharge is based on a per-credit-hour charge. For students taking 7 or more credit hours, the surcharge is 20% of full-time tuition. The following table displays resident undergraduate tuition rates and the surcharge amounts for students taking 7 or more credit hours in FY 2008 by campus:

Table 5

**FY 2008 Arizona University System
Resident Undergraduate Tuition & Threshold Surcharge**

	<u>Tuition Rate</u>	<u>Above Threshold Surcharge</u>
ASU Main	\$4,821	\$964
ASU East & West	4,620	924
NAU	4,595	919
UA Main & HSC	4,824	965

Arizona Board of Regents/University of Arizona College of Medicine – Report on Phoenix Update – Pursuant to a General Appropriation Act footnote, the Arizona Board of Regents (ABOR), with input from the University of Arizona (UA) and Arizona State University (ASU), is required to provide an update to the JLBC on the University of Arizona Phoenix Medical Campus.

ABOR previously submitted a report on the Phoenix Medical Campus on September 15, 2006. The report submitted by ABOR on February 15, 2007 includes updated information on the following topics:

Formal Relationships with Area Hospitals – In December 2006, the College of Medicine entered into a memorandum of understanding (MOU) with Banner Health, under which Banner Health will become the college’s primary academic hospital affiliation in Phoenix. According to the MOU, Banner Health will construct a new teaching hospital on the Phoenix Biomedical Campus and build a new comprehensive cancer center in conjunction with the UA College of Medicine’s Arizona Cancer Center. In addition to their affiliation with Banner Health, the college will establish an academic affiliation with the Maricopa Integrated Health System.

Creation of New Residencies – Once it is operational, the Banner Health teaching hospital will be eligible to establish new residency positions that could be funded under the federal Medicare program. The new cancer center would also add residency positions.

In their August 15th update, ABOR reported that the College of Medicine intended to seek accreditation for 7 or more residency programs scheduled to start in July 2008. The UA College of Medicine now reports that they will seek accreditation for 8 residency programs, of which 6 will start in 2008 and 2 will start in 2009. Once all 8 programs are fully operational in 2012, they will establish an estimated 118 new resident position.

Additional Reporting Requirements – ABOR's report does not include further updates from the August 15th report on the availability of clinical rotations for medical students in the state, the expansion of medical services in the state's rural areas, and their partnerships with private medical schools. In February 2007, the Phoenix program curriculum received accreditation from the Liaison Committee on Medical Education, the accrediting body for the College of Medicine.

Arizona Department of Transportation – Quarterly Report on Motor Vehicle Division Wait Times – The Motor Vehicle Division (MVD) was appropriated an additional 25 FTE Positions in FY 2007 for MVD customer service staff to reduce customer wait time. Laws 2006, Chapter 344, requires the Arizona Department of Transportation to report to the Legislature quarterly on customer wait times in MVD field offices and vehicle registration renewal by mail turnaround times. The number of MVD counter clerks increased by 63, or 9%, from 698 in FY 2006 to 761 in the 1st half of FY 2007, with a resultant decrease in customer wait time from receiving a ticket until arriving at the counter of (8.6) minutes, or (30.9)%, from 27.8 minutes in FY 2006 to 19.2 minutes in the 1st half of FY 2007. A pilot program at 4 MVD offices (South Mountain, Scottsdale, Northwest Phoenix and East Mesa) showed an additional wait time of 6.6 minutes from arrival at the office until receiving a numbered ticket.

Arizona State University – Guaranteed Tuition Pilot Plan – A footnote in the General Appropriation Act requires Arizona State University (ASU) to report to the Joint Legislative Budget Committee by December 1, 2006 on the development of a 4-year pilot program for an optional flat rate tuition for incoming undergraduate students beginning in academic year 2007-2008.

The Arizona Board of Regents (ABOR) approves tuition increases for the upcoming academic year in the fall. As a general guideline, ABOR approves tuition rates that would rank in the top of the bottom third of tuition charged by all other public universities. The flat rate tuition pilot program will allow students to pay a guaranteed yearly tuition rate. The program applies to tuition only, allowing all student fees to be assessed at the same rate. The pilot program will be implemented at all ASU campuses and will be offered for 4-

year, 3-year, and 2-year guarantee periods. Students that choose the flat rate tuition option cannot elect to pay the yearly tuition rate until their guarantee period ends.

The following table displays guaranteed tuition rates at each campus and for each guarantee period in the 2007 – 2008 academic year:

Table 6		
Arizona State University		
Guaranteed Rate Tuition Pilot Program		
	<u>Tempe & Downtown</u>	<u>East & West</u>
4 Year	5,635	5,402
3 Year	5,407	5,183
2 Year	5,189	4,974

By contrast, the 2007-2008 academic year tuition rate at the Tempe and Downtown campuses will be \$4,821 and the tuition rate at the East and West campuses will be \$4,620. These rates would have to increase by 10.5% on average each year for total tuition paid over a 4-year period to equal the total amount of tuition paid under the flat rate option.

Arizona Department of Water Resources – Report on Fee Collections in the Assured and Adequate Water Supply Fund – Pursuant to a FY 2007 General Appropriation Act footnote, the Arizona Department of Water Resources (DWR) is required to report quarterly on the amount of fees collected by the Assured and Adequate Water Supply (AAWS) Program.

Laws 2005, Chapter 217 established the AAWS Administration Fund to provide for the costs of the AAWS Program. New fees were approved in September 2006. Collections in the first quarter of FY 2007 amounted to \$74,500. The collections in the second quarter amounted to \$250,200, making the total collections in the first half of FY 2007 approximately \$324,700. DWR anticipates that the fees will eventually generate approximately \$1,100,000 per year for the operations of the AAWS program.

OTHER ISSUES

Attorney General Settlement Allocation

In 2003, the Attorney General's office successfully prosecuted C.P. Direct, a Scottsdale-based company that marketed nutritional supplements, for fraud and money laundering. As a result of the lawsuit, C.P. Direct forfeited \$28.7 million to the state. Of this amount, the Attorney General's office has allocated \$25.6 million, while \$3.1 million remains unallocated. The allocations to date include:

- \$17.7 million to the Department of Public Safety (DPS) for construction of a new crime lab;
- \$2.2 million to DPS for the detail design phase of a fully interoperable communications system for public safety agencies' communications statewide;

- \$2.1 million to the Arizona Criminal Justice commission for victim compensation;
- \$1.5 million to the Attorney General Anti-Racketeering Fund;
- \$1.4 million to DPS to replace personal computers;
- \$0.7 million to DPS for a tri-agency disaster recovery system;

The Executive's FY 2008 proposed budget had originally included General Fund monies to fund the interoperable communications system, personal computer replacement, and the tri-agency disaster recovery system, while the JLBC Baseline included General Fund monies for only the interoperable communications system. On February 12, 2007, the Joint Appropriations Subcommittee on Transportation and Criminal Justice adopted a motion to specify legislative intent that all 3 of these items be funded with monies from the settlement.

State Appropriations Limit

A.R.S. § 41-1273 requires JLBC Staff to annually report on how state spending compares to the constitutional appropriations limit. The Arizona Constitution limits the appropriation of certain state revenues to no more than 7.41% of Arizona personal income. Under the January JLBC Baseline budget, total FY 2007 state appropriations (both General and Other Funds) would be \$13.79 billion, or 6.83% of personal income. The FY 2008 JLBC Baseline includes spending of \$14.03 billion, which is 6.45% of personal income.

Revenues subject to the limit include: 1) taxes, 2) university collections, and 3) licenses, fees, and permits. These revenues may either be deposited in the General Fund or used for a dedicated purpose. The following appropriated revenues are not subject to the limit: 1) interest and dividends earnings, 2) sales, rentals, and service receipts, 3) federal grants, 4) gifts and donations, and 5) monies received by the state as a trustee, custodian, or agent.

Truth in Taxation K-12 Property Tax Rates

A.R.S. § 41-1276 requires the JLBC Staff to annually calculate and report the Truth in Taxation (TNT) adjustments to the K-12 property tax rates. The K-12 property tax rates consist of the Qualifying Tax Rate (QTR) and the County Equalization Tax Rate; however, the County Equalization Tax Rate was suspended from FY 2007 through FY 2009.

Each year these rates are adjusted to offset increases in the valuation of existing property, with the intended result of producing no change in statewide property tax liability. The following table displays the current rates, as well as the new rates after making the adjustment.

Table 7

K-12 Education Tax Rates

	<u>FY 2007</u>	<u>FY 2008</u>
Unified QTR	\$3.4788	\$3.2040
Non-Unified QTR	\$1.7394	\$1.6020

Based on the most recent information submitted by county assessors, statewide assessed values are expected to increase by 15.2% in FY 2007, of which 6.6% would be due to new construction, and 8.6% would be due to the higher value of existing properties. The TNT adjustment is made to only offset growth in the assessed valuation of existing property.

Since the state share of K-12 education costs depends on the amount of revenues generated from the QTR and the County Equalization Tax Rate, any reduction in these rates requires the state to provide the Arizona Department of Education (ADE) with additional funding. Based on the forecasted growth rate of 5.6% in existing NAV, the FY 2008 JLBC Baseline already included additional funding to ADE. Since actual existing rates grew by 8.6%, the QTR will need to be adjusted lower. As a result, the JLBC Baseline would need to be adjusted upward by \$19.0 million to fund the revised rates. Of this total, \$2.0 million would fund additional Homeowner's Rebate costs resulting from the increase in existing NAV.

State of Arizona

General Fund Revenue: Change from Previous Year and June Forecast January 2007

	Current Month					FY 2007 YTD (Seven Months)				
	Change From					Change from				
	Actual	January 2006		Forecast		Actual	January 2006		Forecast	
	January 2007	Amount	Percent	Amount	Percent	January 2007	Amount	Percent	Amount	Percent
Taxes										
Sales and Use	439,996,411	\$19,714,084	4.7 %	(\$7,048,589)	(1.6) %	\$2,668,311,971	\$201,970,454	8.2 %	\$23,511,471	0.9 %
Income - Individual	544,268,647	82,698,699	17.9	35,623,547	7.0	2,331,342,727	201,816,941	9.5	(6,235,373)	(0.3)
- Corporate	37,266,911	3,260,627	9.6	(1,958,889)	(5.0)	528,174,278	95,399,253	22.0	55,802,378	11.8
Property	(106,275)	(711,450)	--	(106,275)	--	13,383,086	(1,007,117)	(7.0)	(516,914)	(3.7)
Luxury	4,319,994	(1,733,768)	(28.6)	(1,305,006)	(23.2)	42,080,897	4,221,210	11.1	2,705,897	6.9
Insurance Premium	527,737	414,042	364.2	(3,728,263)	(87.6)	144,292,606	6,943,851	5.1	8,736,606	6.4
Estate	2,716	(511,374)	(99.5)	2,716	--	(949,957)	(11,840,631)	--	(1,149,957)	--
Other Taxes	73,441	(4,636)	(5.9)	8,316	12.8	387,711	(10,069)	(2.5)	(68,164)	(15.0)
Sub-Total Taxes	\$1,026,349,582	\$103,126,224	11.2 %	\$21,487,557	2.1 %	\$5,727,023,319	\$497,493,892	9.5 %	\$82,785,944	1.5 %
Other Revenue										
Lottery	2,891,100	(267,100)	(8.5)	(2,908,900)	(50.2)	18,916,400	(5,484,600)	(22.5)	(9,683,600)	(33.9)
License, Fees and Permits	2,893,478	43,965	1.5	(443,222)	(13.3)	25,293,184	6,929,124	37.7	3,537,684	16.3
Interest	10,083,838	3,764,880	59.6	3,483,838	52.8	53,696,097	25,658,909	91.5	19,096,097	55.2
Sales and Services	7,839,672	339,384	4.5	416,272	5.6	28,448,387	(3,333,203)	(10.5)	(2,296,313)	(7.5)
Other Miscellaneous	3,100,966	1,398,526	82.1	1,779,466	134.7	18,709,205	4,768,770	34.2	9,943,705	113.4
Disproportionate Share	0	0	--	0	--	0	0	--	0	--
Transfers and Reimbursements	4,896,696	(7,463,289)	(60.4)	3,196,696	188.0	7,829,593	(8,876,499)	(53.1)	929,593	13.5
Sub-Total Other Revenue	31,705,750	(2,183,634)	(6.4) %	5,524,150	21.1 %	152,892,866	19,662,501	14.8 %	21,527,166	16.4 %
TOTAL BASE REVENUE	\$1,058,055,332	\$100,942,590	10.5 %	\$27,011,707	2.6 %	\$5,879,916,185	\$517,156,393	9.6 %	\$104,313,110	1.8 %
One-Time Revenue										
Urban Revenue Sharing	(45,935,888)	(10,500,144)	29.6	0	0.0	(321,551,216)	(73,501,009)	29.6	0	0.0
Sub-Total Transfers In	(45,935,888)	(10,500,144)	29.6 %	0	0.0 %	(321,551,216)	(73,501,009)	29.6 %	0	0.0 %
TOTAL REVENUE	\$1,012,119,444	\$90,442,446	9.8 %	\$27,011,707	2.7 %	\$5,558,364,969	\$443,655,384	8.7 %	\$104,313,110	1.9 %